

28 February 2020

Consumer Cyclical | Auto & Autoparts

**UMW** (UMWH MK)

**Sell** (From Neutral)

## Triple Threat; Downgrade To SELL

Target Price (Return) MYR2.90 (-10%)  
 Price: MYR3.23  
 Market Cap: USD896m  
 Avg Daily Turnover (MYR/USD) 1.8m/0.43m

- **Downgrade to SELL from Neutral, TP drops to MYR2.90** from MYR4.45, 10% downside. FY19 core earnings missed estimates, on disappointing automotive and equipment numbers. Associate contributions fell, as the depreciation cost of Perodua's new investment kicked in. UMW Toyota SB expects sales to decline this year, from stiff competition. The impending introduction of the X50 also puts Yaris and Vios sales at risk. Recent weakening of the MYR vs USD and JPY has heightened near-term earnings risks. Despite the 28% YTD share price decline, the stock remains overvalued.
- **FY19 numbers a letdown.** UMW's FY19 core earnings of MYR259.1m (-16% YoY) are below our/Street expectations, at 75%/77% of full-year estimates. This is after stripping out the MYR188.1m gain on disposal of the Shah Alam land. Net profit was dragged by lower-than-expected automotive and equipment earnings. Anticipation of seasonally stronger 4Q19 earnings fell, after automotive and equipment EBIT margins deteriorated. A DPS of 2 sen was declared, bringing full-year DPS to 6 sen (FY18: 7.5 sen) including a 4 sen special DPS from the disposal of the Shah Alam land.
- **4Q19 automotive earnings underperformed** after margins contracted, likely due to heavy discounting during the year-end sales. Perodua's associate contribution decreased QoQ and YoY, which we think was due to the depreciation cost of its new investment kicking in. Recent media reports indicate that Perodua is upgrading its factory, including preparing new lines for its new model. We expect competition to further intensify with the introduction of the Proton X50. The model is expected to be priced at MYR75,000-85,000 – which is within the Toyota Vios' and Yaris' pricing range as well (these models accounted for c.50% of UMW Toyota SB's total sales volume in 2019). UMW Toyota SB set a sales target of 66,000 units (2019: 70,009 units) for 2020, while Perodua is anticipating a flattish year, with a target of 240,000 units.
- **Equipment and manufacturing and engineering (M&E) divisions.** UMW's equipment division earnings for FY19 fell on tepid demand and margin compression attributed to the price war. The unit is expected to remain sluggish amidst slower economic growth, with demand being dampened. That said, its M&E segment is the bright spot. The aerospace unit is now profitable, one year ahead of the set timeline, and is expected to continue gaining traction in 2020, as it ramps up production of Rolls-Royce fan cases.
- **Key risks and forecasts.** We cut FY20-21F earnings by 34% and 37%, as we revise down earnings assumptions for the automotive and equipment divisions. A stronger-than-expected MYR against the JPY and USD are key upside risks to our call and earnings forecasts.
- **UMW is now a SELL**, as intense competition in the local automotive market is likely to limit earnings growth. The imminent launch of Proton's anticipated juggernaut – the X50 – will likely see Toyota cede market share in its core B-segment product space. Recent weakening of the MYR vs the USD and JPY also could crimp margins further. The equipment business will continue to remain sluggish in the near term, from the price war. UMW is currently overvalued, at 14.3x P/E (sector average: 12-13x). Our new TP is based on an unchanged 13x target P/E of revised 2020F earnings.

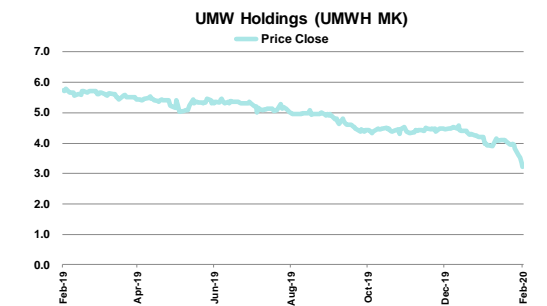
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### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(28.1)	(23.3)	(26.3)	(35.3)	(44.0)
Relative	(22.8)	(19.0)	(21.1)	(30.0)	(31.9)
52-wk Price low/high (MYR)					3.2 – 0.43



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (MYRm)	11,304	11,739	11,454	11,600	11,630
Recurring net profit (MYRm)	308	259	265	267	277
Recurring net profit growth (%)	6.6	(16.0)	2.2	1.0	3.6
Recurring P/E (x)	12.2	14.6	14.3	14.1	13.6
P/BV (x)	1.1	1.0	1.0	0.9	0.9
P/CF (x)	(2.6)	7.1	5.6	9.0	8.9
Dividend Yield (%)	2.3	1.9	1.9	1.9	1.9
EV/EBITDA (x)	148.4	11.3	11.0	11.1	11.2
ROE (%)	6.7	5.2	5.0	4.8	4.7
Net debt to equity (%)	85.8	75.2	68.2	66.1	64.1
Interest coverage (x)	3.4	2.6	3.0	2.5	2.5

Source: Company data, RHB

## Financial Exhibits

Asia	Financial summary	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22
Malaysia	Recurring EPS (MYR)	0.26	0.22	0.23	0.23	0.24
Consumer Cyclical	DPS (MYR)	0.08	0.06	0.06	0.06	0.06
<b>UMW Holdings</b>	BVPS (MYR)	2.86	3.16	3.31	3.47	3.64
Bloomberg UMW MK	ROE (%)	6.71	5.18	4.97	4.78	4.72
<b>Sell</b>						

Valuation basis	Valuation metrics	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22
13x P/E on forward earnings.	Recurring P/E (x)	12.2	14.6	14.3	14.1	13.6
	P/B (x)	1.13	1.02	0.98	0.93	0.89
	FCF Yield (%)	-	-	-	-	-
	Dividend yield (%)	2.3	1.9	1.9	1.9	1.9
	EV/EBITDA (x)	148.4	11.3	11.0	11.1	11.2
	EV/EBIT (x)	23.6	23.1	22.0	21.6	21.5

### Key drivers

- Introduction of attractive new car models;
- Long-term growth potential from aerospace business.

### Key risks

- Weakening of the MYR vs USD and JPY;
- Weaker-than-expected economic growth.

### Company Profile

UMW is the largest company in the automotive sector. Its 51%-owned subsidiary UMW-Toyota imports, assembles and distributes Toyota and Lexus vehicles in Malaysia.

Income statement (MYRm)	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22
Total turnover	11304	11739	11454	11600	11630
Gross profit	3,109	3,228	3,150	3,190	3,198
EBITDA (adj.)	53	679	679	681	679
Depreciation & amortisation	282	(346)	(339)	(332)	(325)
Operating profit	335	333	340	349	354
Net interest	(98)	(126)	(112)	(139)	(140)
Pre-tax profit	593	567	565	560	568
Taxation	(124)	(109)	(113)	(112)	(114)
Net profit	515	447	265	267	277
Recurring net profit	308	259	265	267	277

Cash flow (MYRm)	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22
Change in working capital	(1,104)	(169)	217	(9)	(2)
Cash flow from operations	(1,460)	533	671	421	423
Capex	(915)	(346)	(400)	(400)	(400)
Cash flow from investing activities	(431)	394	(232)	(232)	(232)
Dividends paid	(211)	(165)	(157)	(152)	(149)
Cash flow from financing activities	(145)	(430)	1,319	(52)	(149)
Cash at beginning of period	1,177	(1,291)	(1,387)	272	309
Net change in cash	(1,291)	(1,387)	272	309	250
Ending balance cash	(1,291)	(1,387)	272	309	250

Balance sheet (MYRm)	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22
Total cash and equivalents	1,312	1,472	3,645	3,683	3,624
Tangible fixed assets	2,821	2,757	2,266	2,334	2,409
Total investments	2,062	2,127	2,396	2,678	2,964
Total assets	10,758	11,148	12,609	13,028	13,338
Short-term debt	534	386	386	386	386
Total long-term debt	2,298	2,123	3,600	3,700	3,700
Total liabilities	5,044	5,053	6,219	6,342	6,347
Total equity	5,714	6,094	6,390	6,686	6,990
Total liabilities & equity	10,758	11,148	12,609	13,028	13,338

Key metrics	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22
Revenue growth (%)	2.1	3.9	(2.4)	1.3	0.3
Recurrent EPS growth (%)	6.6	(16.0)	2.2	1.0	3.6
Gross margin (%)	27.5	27.5	27.5	27.5	27.5
Operating EBITDA margin (%)	0.5	5.8	5.9	5.9	5.8
Net profit margin (%)	2.7	2.2	2.3	2.3	2.4
Capex/sales (%)	8.1	2.9	3.5	3.4	3.4
Interest cover (x)	3.4	2.6	3.0	2.5	2.5

Source: Company data, RHB

## Results At a Glance

Figure 1: Earnings review

FYE Dec (MYRm)	4Q18	3Q19	4Q19	QoQ (%)	YoY (%)	FY18	FY19	YoY (%)	Comments
<b>Revenue</b>	<b>2,679.4</b>	<b>2,882.7</b>	<b>3,115.7</b>	<b>8.1</b>	<b>16.3</b>	<b>11,303.6</b>	<b>11,739.1</b>	<b>3.9</b>	Higher, due to the increase in Toyota/Lexus sales.
<b>EBIT</b>	<b>82.9</b>	<b>80.1</b>	<b>75.1</b>	<b>(6.3)</b>	<b>(9.4)</b>	<b>335.2</b>	<b>332.6</b>	<b>(0.8)</b>	
<i>EBIT margin (%)</i>	<i>3.1</i>	<i>2.8</i>	<i>2.4</i>			<i>3.0</i>	<i>2.8</i>		Margin deteriorated due to the depreciation cost of the new Bukit Raja plant.
Finance costs	(53.5)	(30.8)	(32.6)	6.0	(39.1)	(98.3)	(125.9)	28.1	
Associates	100.4	85.2	64.6	(24.2)	(35.7)	270.7	291.6	7.7	Weaker 4Q19 as depreciation cost from Perodua's new investment kicked in.
Investment income	21.5	15.7	16.4	4.4	(23.4)	85.7	68.3	(20.3)	
<b>Pretax profit</b>	<b>151.2</b>	<b>150.3</b>	<b>123.5</b>	<b>(17.8)</b>	<b>(18.3)</b>	<b>593.3</b>	<b>566.6</b>	<b>(4.5)</b>	
<i>Pretax margin (%)</i>	<i>5.6</i>	<i>5.2</i>	<i>4.0</i>			<i>5.2</i>	<i>4.8</i>		
Tax	(11.4)	(21.0)	(21.9)	4.3	91.4	(124.1)	(108.7)	(12.4)	
<i>Eff tax rate (%)</i>	<i>(7.6)</i>	<i>(14.0)</i>	<i>(17.7)</i>			<i>(20.9)</i>	<i>(19.2)</i>		
Discontinued Op	(45.3)	(1.9)	(16.9)	779.6	(62.8)	(176.3)	(17.4)	(90.1)	
MI	(41.2)	(20.9)	(37.6)	79.8	(8.6)	(120.0)	(153.8)	28.1	
<b>Core net profit</b>	<b>81.0</b>	<b>103.3</b>	<b>20.0</b>	<b>(80.7)</b>	<b>(75.3)</b>	<b>308.4</b>	<b>259.1</b>	<b>(16.0)</b>	Below our and Street expectations.
<i>Net margin (%)</i>	<i>3.0</i>	<i>3.6</i>	<i>0.6</i>			<i>2.7</i>	<i>2.2</i>		

Source: Company data, RHB

Figure 2: Earnings review (Segmental breakdown)

FYE Dec (MYRm)	4Q18	3Q19	4Q19	QoQ (%)	YoY (%)	FY18	FY19	YoY (%)	Comments
Automotive	2,046.1	2,296.9	2,450.0	6.7	19.7	8,949.2	9,295.9	3.9	Toyota/Lexus recorded higher sales volume.
Equipment	397.8	353.7	328.0	(7.2)	(17.5)	1,540.2	1,408.2	(8.6)	Heavy equipment faced stiff competition but was partially offset by resilient industrial equipment sales.
Mfg & Eng	242.5	252.4	328.5	30.2	35.5	842.8	1,062.5	26.1	Ramp-up in fan cases production.
Others	(4.5)	(20.3)	9.1	(144.8)	(304.4)	(25.9)	(27.4)	6.0	
<b>Revenue</b>	<b>2,681.8</b>	<b>2,882.7</b>	<b>3,115.7</b>	<b>8.1</b>	<b>16.2</b>	<b>11,306.3</b>	<b>11,739.1</b>	<b>3.8</b>	
Automotive	125.5	140.1	114.9	(18.0)	(8.5)	545.1	530.3	(2.7)	
Equipment	26.0	30.8	27.3	(11.4)	4.7	152.3	135.7	(10.9)	
Mfg & Eng	9.5	15.4	30.0	95.3	216.8	21.6	60.9	182.0	
Others	(57.1)	(35.9)	(48.6)	(35.4)	14.8	(139.9)	(160.3)	14.6	
<b>PBT</b>	<b>103.9</b>	<b>150.3</b>	<b>123.5</b>	<b>(17.8)</b>	<b>18.8</b>	<b>579.2</b>	<b>566.6</b>	<b>(2.2)</b>	
<b>PBT margins</b>									
Automotive	6.1	6.1	4.7			6.1	5.7		4Q19 margin lower likely due to heavy discounting during year-end sales and lower Perodua's contribution
Equipment	6.5	8.7	8.3			9.9	9.6		
Mfg & Eng	3.9	6.1	9.1			2.6	5.7		
Others	1,279.3	176.5	(533.1)			540.3	584.0		
	<b>3.9</b>	<b>5.2</b>	<b>4.0</b>			<b>5.1</b>	<b>4.8</b>		
Automotive	105.0	104.4	82.4	(21.0)	(21.5)	362.7	374.8	3.3	Perodua recorded higher sales volume
Equipment	18.2	23.2	5.5	(76.1)	(69.6)	117.5	87.8	(25.3)	
Mfg & Eng	3.2	9.1	17.9	96.6	462.6	(3.5)	30.5	(964.3)	
Others	(75.6)	(33.3)	(51.1)	53.2	(32.4)	49.4	(164.3)	(432.9)	
<b>NP</b>	<b>50.8</b>	<b>103.3</b>	<b>54.8</b>	<b>47.0</b>	<b>7.9</b>	<b>526.0</b>	<b>328.8</b>	<b>(37.5)</b>	
<b>NP margins</b>									
Automotive	5.1	4.5	3.4			4.1	4.0		
Equipment	4.6	6.6	1.7			7.6	6.2		
Mfg & Eng	1.3	3.6	5.5			(0.4)	2.9		
Others	1,694.0	163.8	(560.0)			(190.7)	598.9		
	<b>1.9</b>	<b>3.6</b>	<b>1.8</b>			<b>4.7</b>	<b>2.8</b>		

Source: Company data

Figure 3: UMW vehicle sales summary

FYE Dec (units)	4Q18	3Q19	4Q19	QoQ (%)	YoY (%)	2018	2019	YoY (%)
<b>Toyota/Lexus</b>	<b>13,058</b>	<b>16,628</b>	<b>21,858</b>	<b>31.5</b>	<b>67.4</b>	<b>66,562</b>	<b>70,009</b>	<b>5.2</b>
- Passenger	7,251	12,313	17,180	39.5	136.9	44,457	53,433	20.2
- Commercial	5,807	4,315	4,678	8.4	(19.4)	22,105	16,576	(25.0)
<b>Perodua</b>	<b>59,040</b>	<b>56,972</b>	<b>61,587</b>	<b>8.1</b>	<b>4.3</b>	<b>227,243</b>	<b>240,341</b>	<b>5.8</b>
- Passenger	59,040	56,972	61,587	8.1	4.3	227,243	240,341	5.8
<b>Total</b>	<b>72,098</b>	<b>73,600</b>	<b>83,445</b>	<b>13.4</b>	<b>15.7</b>	<b>293,805</b>	<b>310,350</b>	<b>5.6</b>

Source: Malaysian Automotive Association

**Figure 4: Historical and forecast assumptions**

<b>FYE Dec</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020F</b>	<b>2021F</b>	<b>2022F</b>
Toyota / Lexus (units)	65,110	70,474	66,562	70,009	66,000	67,000	67,000
Perodua (units)	207,110	204,887	227,243	240,341	236,000	236,000	238,000
FX (JPY/MYR)*	3.82	3.85	3.65	3.80	3.80	3.80	3.80
FX (USD/MYR)*	4.14	4.30	4.04	4.14	4.05	4.05	4.05
<b>*Average rate</b>							

Source: RHB

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